In The

Supreme Court of the United States

October Term, 1976

Supreme Court, U.S.
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No. 76-1359

BANKERS TRUST COMPANY,

Petitioner,

vs.

SAMUEL MALLIS AND FRANKLYN KUPFERMAN,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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TABLE OF CONTENTS

Page

Jurisdiction 1

Questions Presented 1

Argument:

The decision by the Second Circuit does not raise an issue of public importance. 2

Conclusion 5

TABLE OF CITATIONS

Cases Cited:

McClure v. First National Bank of Lubbock Texas, 497 F. 2d 490 (C.A. 5 1974), cert. denied, 420 U.S. 930 (1975) 2, 3, 4

S.E.C. v. Guild Films Co., 279 F.2d 485 (C.A. 2), cert. denied, 364 U.S. 810 (1960) 4

United States v. Gentile, 530 F.2d 461 (C.A. 2), cert. denied, ___ U.S. ___ 4

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This brief is submitted in opposition to the petition for a writ of certiorari to the United States Court of Appeals for the Second Circuit filed by petitioner, Bankers Trust Company.

JURISDICTION

The jurisdiction of this Court is not contested.

QUESTIONS PRESENTED

1. Whether a commercial bank, having received stock as security for a loan may with impunity, fraudulently and with scienter represent to a prospective redeemer of the stock other than the pledgor, that the same has value when it is in fact worthless paper.

2. Whether the anti-fraud provisions of the Federal Securities Laws do not apply to a commercial bank simply because a commercial bank is not primarily in the securities business.

ARGUMENT

The decision by the Second Circuit does not raise an issue of public importance.

The position taken by Bankers Trust Company in its brief in support of the petition for a writ of certiorari is that a pledge of stock, even if induced as a result of fraud, does not fall within the ambit of the anti-fraud provisions of the Federal Securities Laws; and that, *a fortiori,* there can be no fraud when, *without more,* the parties are placed in status quo by a redemption of the pledge. The petitioner then goes on to urge that this is such a case, citing *McClure v. First National Bank of Lubbock Texas,* 497 F.2d 490 (C.A. 5 1974), *cert. denied,* 420 U.S. 930 (1975).

The difficulty with the argument is that the facts do not fit into that mold, but rather into a different mold as to which the opinion in the *McClure* case held that there would be liability.

McClure involved an even more simplistic set of facts then those suggested by the petitioner. There, the plaintiff alleged that she had been fraudulently induced in the original instance to guarantee repayment of a loan; that she pledged stock for an extension of the loan which had in the original instance been fraudulently induced. She sought to be exonerated from her plight although she had not repaid the loan and although the pledgee still held the stock. That is not this case.

Here, such rights as the defendant enjoyed as pledgee were surrendered upon receipt of monies generated by a third party, the plaintiffs. As the opinions of the District Court and the Court of Appeals indicate, the plaintiffs, who were strangers to

all parties until the day of the transaction which gives rise to this litigation, arranged to borrow $156,000 from Franklin National Bank, whose officer attended a closing in their behalf at which time a Franklin National Bank check was delivered to Bankers Trust Company to redeem the stock; the pledge having been redeemed the securities in question were delivered by Bankers Trust Co. to the officer of Franklin National Bank who was acting in behalf of the plaintiffs. It is claimed that the representative of Bankers Trust Company in attendance at the closing affirmatively represented that the securities were valid, sound and subsisting securities and were what they purported to be when in fact the record in the court below establishes without dispute, that Bankers Trust Company was on actual notice from the issuer for at least a year prior to the closing that the securities were worthless. Indeed, the issuer had, about a month prior to the closing, filed a complaint in the Southern District of New York naming Bankers Trust Company as a defendant in an action to recover possession of the worthless securities, but the record does not reflect whether the summons had been served upon Bankers Trust Company prior to the closing.

Nothing in *McClure, supra,* called for a conclusion other than that reached by the Second Circuit in this case. On the contrary, the language of *McClure* supports the conclusion reached by the Second Circuit in this case although this was apparently overlooked by the latter court. The *McClure* court had the following to say about the implications arising from the disposition by a bank of stock originally obtained as a pledge other than by return to the pledgor:

> "If the bank sells the stock pledged as loan collateral, it might then be subjected to liability in connection with the sale if it does not meet the requirements of the anti-fraud provisions of the securities acts, but mere acceptance of a stock pledge as collateral in a privately negotiated transaction between borrower and lender, does

> not, of itself, bring within the scope of the Federal Securities Act a transaction otherwise outside their purview. See 1 L. Loss Securities Regulation, 649 (Second edition, 1961)."

The court then went on to distinguish *S.E.C. v. Guild Films Co.*, 279 F.2d 485 (C.A. 2), *cert. denied*, 364 U.S. 810 (1960), and other cases which found liability under the Securities Laws against a pledgee bank.

While not necessarily germane to the question of whether or not certiorari should be granted in this case, it may nevertheless be observed that the decision by the court in *McClure, supra*, is not inconsistent with the decision reached by the Second Circuit in *United States v. Gentile*, 530 F.2d 461 (C.A. 2), *cert. denied*, ___ U.S. ___ As heretofore observed, the *McClure* case involved the pledge of valid securities as further collateral for a pre-existing loan whose grant had allegedly been fraudulently induced. The fraud related to the loan, not the securities, which were in any event, wholly redeemable by the victimized pledgor. In *Gentile*, the securities pledged were worthless, and the pledgees were fraudulently induced to advance an original consideration in the form of a loan to a pledgor. In this connection, the *McClure* opinion states:

> "We do not doubt that a pledge of securities can constitute a 'sale' in some cases, but we hold that the pledge was not a sale in the circumstances of this case."

None of the cases cited by the petitioner as being inconsistent with the decision by the court below in this case is in fact inconsistent; on the contrary, they are in every respect consistent. The decision of the Second Circuit was eminently correct and supported by all of the authorities and no sound reason exists for this Court to grant certiorari.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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